COMMENTARY ICBC

ICBC's MASSIVE INCREASE TO THE RESERVE FOR PENDING INJURY CLAIMS KEY TO RECENT LOSSES

In the last two years ICBC has set aside some $2.4 billion to increase the previous estimates of the cost to settle claims from prior years. This is a massive increase compared to the adjustments recorded in the last few years, and resulted in the public insurer reporting a cumulative operating loss of $1.5 billion for these two years. This paper examines possible reasons for this extraordinarily large adjustment.

Estimating the Size if the Unpaid Claim Liability

All insurance companies maintain financial reserves to pay for claims that have been received but not yet settled, or for anticipated claims that have not yet been filed. The expected final cost of these claims is calculated by the company's actuary, using Accepted Actuarial Principles (AAP). These are national standards developed by the Actuarial Standards Board of Canada, which are designed to provide a common approach, although judgement by the actuary is also part of the standard.[1]

Estimating the value of the unpaid claim liability involves a variety of assumptions about uncertain future events. In its most recent annual report ICBC notes that: "There is an inherent uncertainty regarding the assumptions to estimate the amount and timing of future claims payments that make up the provision for unpaid claims. The Corporation is liable for all insured events that occurred during the term of the insurance contract, even if the loss is reported after the end of the contract term. In addition, injury claims may take a long period of time to settle."[2]

ICBC also notes that there is a good deal of uncertainty about the ultimate cost of these claims: "The timing of payments of injury claims can be extended due to delayed reporting, and the timing and amount of injury payments can exhibit considerable uncertainty because of the complex bodily injury claims environment, the subjective nature of pain and suffering damages, internal claims operational changes, the judicial environment, and settlement awards."[3]

ICBC stated that provision for unpaid claims can be affected by "the frequency and severity of claims, the discount rate, and **actuarial methods and assumptions**." [my emphasis].[4]

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[1] https://www.cia-ica.ca/docs/default-source/standards/sc022218e.pdf
[2] https://www.icbc.com/about-icbc/company-info/Documents/ar-20.pdf p. 76.
[3] Ibid.
[4] Ibid.

In the Last Two Years ICBC Added $2.4 Billion for Prior Years Claims

Each year ICBC adjusts the reserve for prior years claims to reflect changes to the original assumptions. A change to the reserve for prior years claims will either increase or decrease the annual claims cost, and the net income. Table 1 shows that during the last two years ICBC increased the reserve by $2.40 billion, mostly for Basic claims.

TABLE 1 – PROVISION FOR PRIOR YEAR CLAIMS ($=million)

	2017/18	2018/19	2019/20	3 Yr. Total
Basic	218.2	718.2	757.2	1,475.4
Optional	344.8	503.2	422.7	925.9
Total	563.0	1,221.4	1,179.9	2,401.3

Source: ICBC annual reports.

In the same period the net operating losses totalled $1.53 billion. Table 2 shows the reported net operating loss, and the net loss or gain if the provision for prior years claims were excluded. Excluding the large increase in the provision for prior years claims ICBC would have eliminated the loss for 2018/19 and would have recorded a substantial profit for both the Basic and Optional programs in 2019/20.

TABLE 2 –NET OPERATING LOSS ($=million)

	2017/18	2018/19	2019/20
Basic	(996.5)	(862.2)	(263.4)
Optional	(328.6)	(285.4)	(112.2)
Combined	(1,325.1)	(1,153.6)	(375.6)
Excl. Prior Years Adj.	(563.0)	(1,221.4)	(1,179.9)
Adjust. Net Income	(762.1)	68.8	804.3

Source: ICBC annual reports.

Why Did ICBC Significantly Increase the Provision for Prior Years Claims?

In 2018/19, ICBC set aside $1.22 billion to increase the estimate for claim costs arising from prior years, and increase of almost $660 million over the prior year's adjustment. ICBC explained this increase as funding an unexpected increase in large injury claims, and an increase in the time required to settle the claims.[5] No data was provided to justify this assertion.

In 2019/20, ICBC set aside an additional $1.18 billion for claims from prior years. ICBC justified this major adjustment as including the cost of reversing the previous claimed saving from restricting the number of expert reports (as per the Crowder decision), a decrease in the discount rate, and "increased cost pressure on claims under the full tort system, in particular an increase in the estimated number of large injury claims that will develop over time…."[6]

ICBC did not quantify the one-time savings reversal of the exert reports, but it is likely in the order of $450 million which was recorded as a savings in the prior years' claims adjustment in 2018/19.[7]

Providing for Claims Not Filed

The reference to large injury claims "that will develop over time" hints at a major component of the large allowance for prior years claims; an actuarial adjustment for potential future claims. Each year ICBC must set aside a reserve for claims that have been filed but not settled, as well as for potential claims which may be filed at a future date. The vast majority of both of these types of filings are for injury claims.

In 2018/19 and especially in 2019/20, ICBC dramatically increased its provision for unpaid claims liability (UCL) for potential claims that may be filed. Table 3 shows the year-end total unpaid claim liability for the last three years, split between filed claims ("notified') and not reported claims.

TABLE 3 – YEAR-END UNPAID CLAIM LIABILITY ($=million)

	2017/18	2018/19	2019/20	2 Yr. Increase
Notified	8,480.0	9,378.2	9,518.7	1,038.7
Not Reported	3,415.7	4,909.7	6,485.0	3,069.3
Total	11,895.7	14,287.9	16,003.7	4,108.0

Source: ICBC annual reports.

A review of the relative ratio of notified and not reported claims for the last five years shows that the large increase in the not reported category is an anomaly (see Appendix

[5] https://www.icbc.com/about-icbc/company-info/Documents/ar-19.pdf p. 27.
[6] https://www.icbc.com/about-icbc/company-info/Documents/ar-20.pdf p. 26-27.
[7] See http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_icbc_400_million_27_october_2019/pdf/commentary_icbc_400_million_27_october_2019.pdf

Table A2). Is there data to support the recent large growth in the provision for the cost of injury claims that have not been reported or filed?

1) Have the number of injury claims/exposures significantly increased in recent years?

Recently released claims data shows that injury claims peaked in 2017/18 (50,025) then declined in 2018/19 and 2019/20, while exposures peaked at 78,000 in the same year then declined as well.[8] There is no evidence that the number of injury claims are increasing.

2) Is the Number and Average Cost of Settled Injury Claims Increasing?

In 2017/18, the average cost of a settled litigated (filed in the Supreme Court) injury claim was approximately $107,400. This increased to approximately $128,650 in 2019/20, an increase of approximately 19.8%.[9]

During the same period, the number of settled injury exposures declined from 62,000 to 50,000. The number of settled litigated exposures declined from 17,000 to 15,000.[10]

3) Is the Number of Pending Injury Claims Increasing?

Perhaps the large increase in the provision for prior years claims costs can be partly justified by the 18% increase in the number of pending injury claims reported during the last two years.[11] Had the number of pending injury claims remained at the 2017/18 level, and using an average payment of $42,000 per claim,[12] the hypothetical savings would have been approximately $630 million of the $4.1 billion increase in the unpaid claim liability for the last two years.

[8] http://www.bcpolicyperspectives.com/media/attachments/view/doc/occasional_paper_no_74_icbc_statistical_summary_9_november_2020/pdf/occasional_paper_no_74_icbc_statistical_summary_9_november_2020.pdf Table 3.2.
[9] Ibid. Table 3.6.1
[10] Ibid. Table 3.6
[11] Ibid. Table 3.4.
[12] See tables 3.4 and 3.5 in http://www.bcpolicyperspectives.com/media/attachments/view/doc/occasional_paper_no_74_icbc_statistical_summary_9_november_2020/pdf/occasional_paper_no_74_icbc_statistical_summary_9_november_2020.pdf

From March 2017 to March 2018, ICBC estimated that it would increase its claims handling staff by approximately 20% (134 FTEs).[13] Why with this additional staff, and in light of the decline in injury claims filed, there has been an increase in the number of pending injury claims during the last two years is question for another day.

4) Why the Large Increase in the Provision for Not Reported Claims?

Despite the exceptionally large increase in the provision for potential (not reported) future claims (Table 3), ICBC did not explain what prompted the adjustment. Clearly, actuarial judgement was used to inflate the unpaid claim reserve, but no explanation was offered on what prompted the internal and external auditors to set aside such a large allowance for potential claims.

The move to a hybrid tort liability model as of 1 April 2019 was a significant change in how injury claims of lower values ("minor" injuries) were to be funded and adjudicated if disputed. On 6 February 2020, the government announced that it would legislate a no-fault liability model effective 1 May 2021. Did the ICBC actuary believe that these changes would result in a large number of expensive injury claims being filed at some future date?

5) Is There a Problem With ICBC's Reserving Methodology?

Such large increases in the reserve estimates for claims from prior years suggest that there is a major problem with ICBC's system for claims estimating. The reserving methodology used to develop budgets, and rate requests to the regulator of the compulsory Basic program, appears to be flawed. Tables A1 and A2 show the wide discrepancy between the budgets and the actual adjustments for the last five years for which data is available.

Summary

The $2.4 billion increase in the adjustment for prior years claims during ICBC's last two fiscal years was a primary reason for the cumulative $1.53 billion operating loss reported for these years, and the resulting elimination of the policyholders' capital (equity) reserves.

Given the major increase in the provision for prior years claims, and especially the large increase for potential future claims, one would expect ICBC to explain the rationale for the large adjustment. Unfortunately, no real explanation or justification was provided. Clearly, ICBC's actuaries were using their discretion (actuarial judgement) to pump up

[13] BCUC, ICBC RRA 2019, IR 1, RM.3.11, https://www.bcuc.com/Documents/Proceedings/2019/DOC_53549_B-2-ICBC-Responses-to-BCUC-Intervener-IR1.pdf Pdf 793/1357.

the claims liability, but the absence of any detailed justification allows for speculation as to whether there might be a reversal, or a positive adjustment, to boost the net income in the near future.

 http://www.bcpolicyperspectives.com/

The writer is a retired senior BC government public servant whose paper describing the BC government's manipulation of the finances of BC Hydro from 2008 to 2014 was published by *BC Studies* in November 2016. *BC Studies* published his paper on the 40-year financial history of ICBC in 2013. He was an intervener in the BC Utilities Commission's recent reviews of ICBC's and B.C. Hydro's rate requests.

APPENDIX

Beginning in 2015, ICBC provided the budget for the adjustment for prior years claims in its annual service plan. Table A1 shows that it forecast reductions in each year except 2019/20.

TABLE A1 – BUDGET for ADJUSTMENT for PRIOR YEARS CLAIMS ($=million)

	2015	2016/17	2017/18	2018/19	2019/20
Prior Years Claims	(8)	(24)	(63)	(76)	29

Source: ICBC service plans. Prior to 2015 the budget for the prior years adjustment was included in the total claims cost budget.

However, the actual amounts were radically different, as shown in Table A2. From 2010 to 2013 there were positive (negative) adjustments. Then beginning in 2014 to 2016/17 the amounts of additions to the claim reserve began to increase. Massive increases occurred during the last three years.

TABLE A2 – ACTUAL ADJUSTMENT for PRIOR YEARS CLAIMS ($-million)

2010	2011	2012	2013	2014	2015	2016/17	2017/18	2018/19	2019/20
(2.0)	(14.4)	(69.2)	(54.4)	181.5	244.1	202.6	563.0	1,221.4	1,179.9

Source: ICBC annual reports.

Table A3 shows the growth in the unpaid claim liability separated between known and unknown claims. The last two years witnessed a large increase in the provision for unknown (incurred but not reported) claims, while the increase in the notified category moderated.

TABLE A3 – UNPAID CLAIM LIABILITY ($=million)

	2014	2015	2016/17	2017/18	2018/19	2019/20
Notified	4,662	5,334	6,875	8,480	9,378	9,519
Per Cent	18.0	14.4	28.9	23.3	10.6	1.5
Not Reported	3,544	3,749	3,643	3,416	4,910	6,485
Per Cent	(0.5)	5.8	(2.8)	(6.2)	43.7	32.1
Total	8,206	9,083	10,518	11,896	14,288	16,004
Per Cent	9.2	10.7	15.8	13.1	20.1	12.1

Source: ICBC annual reports.